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1321 Biltmore Hotel

Los Angeles, Calif.

REPORT OF SECTION ON PUBLIC
FINANCE AND TAXATION

- ON -

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BALLOT MEASURE NO. 4, INITIATIVE
CONSTITUTIONAL AMENDMENT REPEALING STATE INCOME TAX

TO BE SUBMITTED TO VOTERS ON STATE OF
CALIFORNIA AT GENERAL ELECTION ON NOVEMBER 3, 1942

SEPTEMBER 18, 1942

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T O W N H A L L

REPORT OF THE SECTION ON PUBLIC FINANCE AND TAXATION ON THE QUESTION OF WHETHER THE CALIFORNIA STATE INCOME TAX SHOULD BE REPEALED

The Section on public finance and taxation has considered the question as to whether the California personal income tax should be repealed and now submits its report. Proponents and opponents of the proposed initiative constitutional amendment to repeal the tax were heard by the Section.

Proposition No. 4 on the ballot at the general State election on November 3, 1942, proposes (1) to repeal the California personal income tax and (2) to prohibit the California legislature from reimposing such a tax without a vote of the people.

The State constitution has contained a specific provision authorizing income taxes since 1879. The present income tax was enacted in 1935 and is generally considered to be an outgrowth of the so-called Riley Stewart tax plan approved by the voters of the State in 1933. It will be recalled that, under this plan, commencing in 1935 the State discontinued the collection of gross receipt taxes on public utilities and the property of these companies was returned to the local tax rolls; also the State assumed additional costs of the schools formerly borne by the counties and the tax on intangibles was eliminated except as applied to solvent credits. The legislature found it necessary to levy new or increased State taxes including a sales tax, and a personal income tax. The personal income tax was modeled generally after the Federal income tax as it existed at that time and the rates were fixed at approximately one-fourth of the Federal schedule. The rates have not been changed and the provisions of the law have remained substantially the same.

In 1936 a proposition appeared on the ballot which proposed to repeal this tax and was defeated by a vote of approximately 1,200,000 to 750,000.

The following tabulation shows the approximate annual yield of the California income tax as compared to total general fund revenues. (Source - California State Chamber of Commerce)

<u>Fiscal Year</u>	<u>Total General Fund Revenues</u>	<u>Personal Income Tax Collections</u>	<u>Ratio of Income Tax to Total Revenues</u>
1936-37	\$158,915,135.	\$16,859,895.	10.6%
1937-38	175,202,337	21,519,037	12.3%
1938-39	166,771,481	20,509,860	12.3%
1939-40	173,449,175	19,570,167	11.3%
1940-41	195,225,147	20,293,440	10.4%
1941-42	237,568,298	29,033,182	12.2%

During the taxable year 1941 approximately 491,000 persons paid personal income taxes to the State. Of these approximately 422,000 reported net incomes under \$5,000 and 243 reported net incomes in excess of \$100,000. These 243 paid total taxes of approximately \$3,700,000 as compared with total taxes of approximately \$3,300,000 paid by the 422,000 reporting incomes under \$5,000.

REPORT OF THE LEGISLATIVE COMMITTEE ON FINANCE AND TAXATION
ON THE QUESTION OF WHETHER THE CALIFORNIA INCOME
TAXES SHOULD BE INCREASED

The Committee on Finance and Taxation has considered the question as to whether the California income taxes should be increased and has the honor to report. It reports and recommends that the proposed legislative committee amendments to increase the tax rates be rejected.

Proposition 13, passed on the ballot at the general election on November 3, 1975, requires that the California personal income tax and the California corporation tax rates be reduced to the rates in effect in 1975.

The State Constitution also contains a provision which prohibits the Legislature from increasing the tax rates on personal income taxes, corporation taxes, or the sales tax. The Committee has considered the question of whether the California income taxes should be increased and has the honor to report. It reports and recommends that the proposed legislative committee amendments to increase the tax rates be rejected.

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The following table shows the estimated annual yield of the California income tax as compared to total general fund revenues. (Source: California State Department of Finance)

Fiscal Year	Total General Fund Revenues	Personal Income Tax Collections	Ratio of Income Tax to Total Revenues
1976-77	\$166,815,100	\$16,800,000	10.1%
1977-78	170,500,000	17,000,000	10.0%
1978-79	174,000,000	17,200,000	9.9%
1979-80	177,500,000	17,400,000	9.8%
1980-81	181,000,000	17,600,000	9.7%
1981-82	184,500,000	17,800,000	9.6%

During the taxable year 1975 approximately 401,000 persons paid state income taxes in the State. Of these approximately 325,000 reported net income under \$5,000 and 515 reported net income in excess of \$10,000. These 515 paid total

The present fiscal condition of the State is improved, the fiscal surplus as of June 30, 1942, being reported as \$14,000,000 and the improvement during the 1941-42 fiscal year being reported as approximately \$75,000,000. It is estimated that, under the present tax laws and budget the surplus of the State will increase at an annual rate of from 60 to 75 million dollars.

The rates of tax imposed by California are among the highest among thirty States imposing income taxes. The following tabulation illustrates the amount of income tax imposed by several States upon various incomes:

State	Tax on Incomes of		
	\$5,000.	\$20,000.	\$100,000.
Arizona	\$67	\$ 692	\$ 4,292
California	50	500	7,950
Illinois	-	-	-
Massachusetts	75	300	1,500
Missouri	95	665	3,865
New York	160	1,150	6,750
North Dakota	90	1,865	13,865
Wisconsin	82	957	6,557

The arguments advanced in favor of repeal of the tax may be summarized as follows:

(1) The financial condition of the State no longer requires the imposition of this tax in order to meet its expenditures.

(2) The increase in Federal individual income taxes emphasizes the burden of double taxation and increases the desirability for the State to withdraw from this field of taxation.

(3) Repeal of the State income tax would help to retain substantial residents within the State and would encourage prospective substantial residents to come to California.

(4) The Act is onerous and inequitable in its terms.

(5) Many individuals believe that administrative and judicial decisions under the Act have been largely against the taxpayers and have strained the words of the Act to impose additional taxes.

(6) Attempts to secure relief for the taxpayers by means of legislation have been fruitless.

(7) Repeal of the Act by initiative is the only practical way of solving the problem.

(8) Repeal of the tax by constitutional amendment will prevent reimposition of the tax without a vote of the people.

(9) It is desirable to keep the state government poor to prevent extravagant expenditures.

The arguments advanced against repeal of the tax may be summarized as follows:

(1) The proposed initiative measure places in the constitution a specific prohibition against the levy of an income tax without the vote of the people.

(2) Because of possible reductions in future collections of sales and gasoline taxes the anticipated surplus may never be realized.

(3) Repeal of the personal income tax would probably preclude reduction of other forms of taxes which might be accomplished by a general program of tax reduction.

(4) The income tax is a companion tax to the sales tax and should be retained to "distribute the burden of tax in accordance with the ability to pay."

(5) The argument that the tax should be repealed because it represents double taxation would be equally valid in the event of a Federal sales tax which is regarded as more than a possibility.

(6) The proper method of correcting alleged onerous and inequitable terms of the law or alleged inequitable administration is by legislation - not by constitutional amendment.

(7) Any excess of income to the State over expenditures during the war period might be invested in United States government bonds instead of reducing taxes, thus providing a fund to finance the State in the post-war period when it may be expected that revenues will decline.

(8) The argument that repeal of the tax would encourage emigration to the State of wealthy individuals is greatly exaggerated.

(9) Because the income tax affects a relatively small number of residents of California, it would be fairer to reduce other taxes than to repeal the income tax.

(10) To reduce taxes equitably, the legislature should reduce both the sales tax and personal income tax and, at the same time, a reduction in the bank and corporation franchise tax would seem desirable.

(11) The proposed initiative amendment does not provide for restoration of the tax on intangibles which was abolished when the income tax was enacted.

(12) The provisions of the measure which require a referendum before future enactment of a personal income tax violate the theory that revenue measures should not be subject to referendum.

(13) The provisions of the proposed amendment which provide for a treatment of income taxes different from the treatment of other taxes increase the danger of a State ad valorem tax on real estate in the event of a future State fiscal emergency.

J. R. WHITE
Chairman

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